No. 95-244

(6)

IN THE
Supreme Court of the United States
OCTOBER TERM, 1995

CHUCK QUACKENBUSH, INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, IN HIS CAPACITY AS LIQUIDATOR AND TRUSTEE OF THE MISSION INSURANCE COMPANY TRUST, MISSION NATIONAL INSURANCE COMPANY TRUST, ENTERPRISE INSURANCE COMPANY TRUST, HOLLAND-AMERICA INSURANCE COMPANY TRUST AND MISSION REINSURANCE CORPORATION TRUST,
Petitioner,

v.

ALLSTATE INSURANCE COMPANY,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF FOR THE PETITIONER

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QUESTIONS PRESENTED

1. Whether the court below erred in holding that a remand order based on abstention is reviewable by appeal under the collateral order doctrine developed in *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949).

2. Whether the court below erred in holding that the abstention powers of federal courts are limited to actions in equity, or alternatively, whether that court erred in limiting the exercise of *Burford* abstention solely to actions in equity.

PARTIES TO THE PROCEEDINGS AND RULE 29.1 STATEMENT

The Appellee in the Ninth Circuit, who is the Petitioner here, is Chuck Quackenbush, the Insurance Commissioner of the State of California (statutory successor to John Garamendi) in his capacity as Liquidator and Trustee of the Mission Insurance Company Trust, Mission National Insurance Company Trust, Enterprise Insurance Company Trust, Holland-America Insurance Company Trust, and Mission Reinsurance Corporation Trust.* The Appellant in the Ninth Circuit, and Respondent here, is Allstate Insurance Company.

* Prior to receivership, the parent of Mission Insurance Company was Mission Insurance Group, Inc. ("MIG"). MIG emerged from Chapter 11 bankruptcy as Danielson Holding Corporation.

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BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A) is reported at 47 F.3d 350. The unpublished order of the district court granting abstention under the *Burford* doctrine is reproduced in Pet. App. B. The unpublished order of the court of appeals denying the petition for rehearing in reproduced in Pet. App. C.

JURISDICTION

The opinion of the court of appeals was entered on February 2, 1995. A timely petition for rehearing with

a suggestion for rehearing *en banc* was denied on May 19, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The statutes involved are the pertinent provisions of the McCarran-Ferguson Act, codified at 15 U.S.C. §§ 1011-1015, the pertinent provisions of the California Insurance Code, codified at Cal. Ins. Code §§ 900-900.2, 900.9, 903-903.5, 905-911, 922.1-923.5, 925, 925.2, 925.4, 1010-1042, 1056.5-1064.12 (Pet. App. D), Federal Rules of Civil Procedure 2, 8(e)(2), 18 and 54(c) (Br. App. A),[1] codified at Title 28, United States Code, and the pertinent provisions of the Judiciary Act, codified at 28 U.S.C. §§ 1332(a), 1441(a),(c)(Pet. App. D) and 1447(c), (d), (Resp. App. 2).

STATEMENT OF THE CASE

1. The Mission Companies[2] are property casualty insurers in liquidation proceedings in California state court. Petitioner, the Insurance Commissioner of the State of California (the "Commissioner")[3] is the court-appointed liquidator. Respondent Allstate Insurance Company ("Allstate") is a reinsurer of the Mission Companies and was also a reinsured of Mission Insurance Company.[4] The particular case before this Court is best understood if it is first placed in the context of the larger proceedings

[1] All references to "Rule" or "Rules" are to the Federal Rules of Civil Procedure unless stated otherwise.

[2] Mission Insurance Company, Mission National Insurance Company, Enterprise Insurance Company, Holland-America Insurance Company and Mission Reinsurance Corporation (the "Mission Companies").

[3] There have been four Commissioners in charge of these proceedings: Commissioner Bruce Bunner, Commissioner Roxani Gillespie, Commissioner John Garamendi, and Commissioner Chuck Quackenbush. Unless there is a reason to do so, this brief will not distinguish the successive Commissioners and will simply refer to the "Commissioner."

[4] *See* note 17 *infra*.

of which it is an essential part. This larger context is discussed in paragraphs 2-16, below, and the details of this case and its specific procedural history are described beginning at paragraph 17 of this Statement.

2. The Mission Companies were placed into California state court conservation proceedings in 1985 (the "Receivership Proceedings"). Vigorous efforts toward rehabilitation ultimately failed, primarily due to the refusal of the Mission Companies' reinsurers to pay the sums due (the "Reinsurance Recoverables") on various reinsurance arrangements. The conservation proceedings were, therefore, converted into liquidation proceedings on February 24, 1987.[5] This was the largest insurance insolvency in United States history up to that time and involved policyholders in all 50 states.[6]

3. California, like all states, has a comprehensive statutory scheme for insurance insolvency matters. The California statutes require that the Commissioner be appointed conservator or liquidator of insolvent insurers, Cal. Ins. Code §§ 1011, 1016, and in that capacity, the Commissioner acts as receiver and trustee. Cal. Ins. Code § 1057; *Anderson v. Great Republic Life Ins. Co.*, 41 Cal. App. 2d 181, 188, 106 P.2d 75, 79 (1940). As receiver, the Commissioner is not simply a common law receiver, but acts in his official capacity as an officer of the state, and is the embodiment of the state's police power in the insurance insolvency context. Cal. Ins. Code §§ 1011, 1059; *20th Century Ins. Co. v. Garamendi*, 8 Cal. 4th 216, 240, 878 P.2d 566, 580, 32 Cal. Rptr. 2d 807, 821 (1994), *cert. denied*, 115 S. Ct. 1106 (1995); *Carpenter v. Pacific Mut. Life Ins. Co.*, 10 Cal. 2d 307, 329, 74 P.2d 761, 774-75 (1937), *aff'd sub nom. Neblett*

[5] Pet. App. E p. 119a-121a, Jt. App. p. 23-34.

[6] MIG, the ultimate corporate holding company, and several non-insurance affiliates were placed into federal bankruptcy proceedings. Although proceedings have occurred in both courts, the bankruptcy court and the Superior Court of the State of California, County of Los Angeles (the "Receivership Court") have completely avoided any jurisdictional conflict.

v. Carpenter, 305 U.S. 297 (1938). At the commencement of insolvency proceedings, title to all assets of the insurer, including all accounts receivable, is vested, by operation of law, in the Commissioner in his official capacity. *See Carpenter*, 10 Cal. 2d at 329, 74 P.2d at 774-75; *Commercial Nat'l Bank v. Superior Court*, 14 Cal. App. 4th 393, 398, 17 Cal. Rptr. 2d 884, 886 (1993); Cal. Ins. Code §§ 1011, 1064.2(b). The underlying proceedings are *in rem* or, alternatively, *quasi in rem*. *Lion Bonding & Sur. Co. v. Karatz*, 262 U.S. 77 (1923); *Penn Gen. Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935); *United States v. Bank of New York & Trust Co.*, 296 U.S. 463 (1936); *Princess Lida v. Thompson*, 305 U.S. 456 (1939).

4. California's integrated statutory plan treats the conservation and liquidation of insurers as a single special proceeding before a single court.[7] A conservation proceeding seeks to preserve and rehabilitate the insurer. If such efforts fail, the proceeding is converted to a liquidation proceeding before the same court.[8] The Commissioner exercises substantial discretion, under the auspices of the state court, in conducting insurance insolvency proceedings. The vital public interest is involved.[9] The insurance industry is a traditional state enclave, and Congress has mandated that it will remain a state enclave, both by its enactment of the McCarran-Ferguson Act[10] and by its exemption of insurance companies from the Federal Bankruptcy Act.[11]

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[7] Under California law, insurance insolvency proceedings are "special proceedings." *Carpenter*, 10 Cal. 2d at 327, 74 P.2d at 773; *Anderson*, 41 Cal. App. 2d at 188-89, 106 P.2d at 79.

[8] *See* Cal. Ins. Code §§ 1016, 1017.

[9] *German Alliance Ins. Co. v. Lewis*, 233 U.S. 389 (1914); *Osborn v. Ozlin*, 310 U.S. 53 (1940); *California State Auto. Ass'n Inter-Ins. Bureau v. Maloney*, 341 U.S. 105 (1951).

[10] 15 U.S.C. §§ 1011-1015.

[11] 11 U.S.C. § 109(b)(2), (d). By exempting insurance insolvencies from federal bankruptcy, Congress deferred to established state processes.

5. The issues in the Receivership Proceedings and in related litigation are intimately connected with California's public policy. For example, the dispute with Allstate requires the interpretation of various reinsurance agreements between the insolvent Mission Companies and Allstate on the one hand, and Mission Insurance Company ("MIC") and Allstate's affiliate Northbrook Excess and Surplus Company ("Northbrook") on the other hand. Allstate reinsured various Mission Companies under certain reinsurance contracts and was reinsured by MIC under separate contracts. Northbrook was reinsured by MIC on still other contracts, but did not reinsure MIC. Allstate seeks to combine sums due to it with sums due to Northbrook and set the total off against the amount Allstate owes to MIC. Northbrook owes nothing to MIC, therefore, it has nothing against which to set off its credit. The Commissioner has determined this combination is impermissible under the statutes and under California law. Allstate also asserts the right to arbitrate the dispute pursuant to clauses in some, but not all, of the agreements. Whether arbitration is available post-liquidation is an unsettled question under California law. The application of the arbitration clause is further complicated, post-liquidation, by the "insolvency clause"[12] contained in the contracts and by the statutory claims process. These issues are also unsettled under California law. Similar disputes exist with other reinsurers.[13] These issues transcend the instant dispute and impact core aspects of the liquidation proceedings and all other Cali-

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[12] Jt. App. p. 109-110.

[13] *See, e.g.*, a March 8, 1994 Order of the Receivership Court (Jt. App. p. 165-166) regarding reinsurance offset rights and the proper interpretation of the decision in *Prudential Reinsurance Co. v. Superior Court (Garamendi)*, 3 Cal. 4th 1118, 842 P.2d 48, 14 Cal. Rptr. 2d 749 (1992) [hereinafter *Prudential*], which order was appealed and is now pending in the case titled *Imperial Casualty and Indemnity Co. v. Insurance Commissioner of the State of California*, California Court of Appeal, Second Appellate District, Case No. B083725 [hereinafter *ICIC*].

fornia insurance insolvencies with similar circumstances.[14] Related litigation that has occurred in the Receivership Proceedings has resulted in decisions by the California Courts of Appeal [15] and the California Supreme Court.[16] In *Prudential*, the California Supreme Court rendered a 4-3 opinion involving the highly disputed and complex issue of when, under California statutory law, a reinsurer may set off claims against the insolvent from the reinsurance recoverables. The determination was that certain offsets (to which the parties now refer as "group-to-group") are not permitted, but that others (to which the parties now refer as "company-to-company") are permissible. Allstate's offset claims involve the correct application and interpretation of the *Prudential* decision. The underlying suit is not a run-of-the-mill contract dispute or collection action. The issues involved require a comprehensive resolution which considers California's statutory scheme and applies the state's public policy.

6. The Commissioner must receive and determine many thousands of claims (including those of Allstate)[17]

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[14] *See, e.g., Doughty v. Underwriters At Lloyd's, London*, 6 F.3d 856, 858, 866 (1st Cir. 1993), where the First Circuit affirmed the remand of a dispute very similar to the instant case, which also left open the arbitration issue. That court referred to the merits of that case as "a veritable hothouse of efflorescent questions" which it left to the state forum. *See also, Corcoran v. Ardra Ins. Co., Ltd.*, 842 F.2d 31, 37 (2nd Cir. 1988).

[15] *Prudential Reinsurance Co. v. Superior Court*, 216 Cal. App. 3d 1321, 265 Cal. Rptr. 386 (1989); *Garamendi v. Mission Ins. Co. (Carboline)*, 15 Cal. App. 4th 1277, 19 Cal. Rptr. 2d 190, *rev. denied* (1993); *ICIC* (pending).

[16] *Prudential*, 3 Cal. 4th 1118.

[17] Allstate's claims filed in the Receivership Proceedings assert the same issues it now seeks to assert in the underlying dispute. Allstate entered into approximately 15 reinsurance treaties and numerous facultative certificates pursuant to which Allstate reinsured one or more of the Mission Companies and balances are due thereunder. Allstate was, in turn, reinsured by MIC under approximately 14 different treaties. In addition, Northbrook, an Allstate affiliate, was reinsured by MIC under approximately 8 completely

which have been filed in the Receivership Proceedings pursuant to state statutes. *See, e.g.*, Cal. Ins. Code §§ 1021, 1032, 1037(c). The Commissioner must also protect, marshal, and eventually liquidate the assets of the Mission Companies. The Commissioner must adjudicate claims under California's claims statutes and distribute the assets under California's priority statutes. Cal. Ins. Code §§ 1033, 1035.5. These are key functions of the Commissioner under the state statutory plan, and the Commissioner is given wide discretion and authority in this regard. *See. e.g.*, Cal. Ins. Code § 1037; *Garris v. Carpenter*, 33 Cal. App. 2d 649, 92 P.2d 688, 692 (1939); *In re Executive Life Ins. Co.*, 32 Cal. App. 4th 344, 38 Cal. Rptr. 2d 453, *rev. denied* (1995). The marshaling and control of the insurer's assets is particularly important in the case of property and casualty companies, such as the Mission Companies, because the large majority of a property and casualty insurer's assets are normally held in the form of accounts receivable.[18]

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different reinsurance agreements. In 1987, Allstate filed several claims in the Receivership Proceedings, seeking to combine all of these various relationships for offset purposes (Jt. App. p. 151-164). By the filing of these proofs of claim, Allstate subjected itself to the *in personam* jurisdiction of the Receivership Court, even assuming *arguendo* that it was not already subject to the Receivership Court's jurisdiction. *See* Cal. Code Civ. Proc. § 410.50(a). The underlying suit includes actions at law under the reinsurance arrangements, but it also involves a declaratory judgment action by the Commissioner, as well as offset claims by Allstate. (Jt. App. p. 35-61). Under California law, a declaratory judgment action is equitable in nature, *Westerholm v. 20th Century Ins. Co.*, 58 Cal. App. 3d 628, 632, 130 Cal. Rptr. 164, 166 n.1 (1976); *Culbertson v. Cizek*, 225 Cal. App. 2d 451, 462, 37 Cal. Rptr. 548, 553 (1964), and the claims for offset are actions "in equity." *Prudential*, 3 Cal. 4th at 1124, 842 P.2d at 50-51, 14 Cal. Rptr. at 751-52.

[18] This Court recognized the importance of permitting such control in *United States v. Bank of New York & Trust Co.*, 296 U.S. 463, 477 (1936) where, in speaking of state court receivership proceedings it said: "In both these cases the proceedings in the state court were *quasi in rem*. Control of the funds was essential

That is true in this case as to the Reinsurance Recoverables.

7. The Receivership Court has, continuously assumed and expressly exercised sole and exclusive jurisdiction over all assets of the Mission Companies "of any kind or nature however and wherever situated, to the exclusion of all other courts." [19] The Receivership Court also issued injunctions forbidding interference with the Commissioner or the proceedings, the institution or prosecution of any actions or proceedings against the insurers or their assets or against the receiver, except after obtaining permission from the Receivership Court. These

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to the exercise of the court's jurisdiction to protect the rights of claimants. . . . The principle, applicable to both federal and state courts, that the court first assuming jurisdiction over property may maintain and exercise that jurisdiction to the exclusion of the other, is not restricted to cases where property has been actually seized . . . [i]t *applies as well where suits are brought to marshal assets*, administer trusts, or liquidate estates, in suits of a similar nature, where, to give effect to its jurisdiction, the court must control the property." (emphasis added) (citing *Farmer's Loan & Trust Co. v. Lake S.E.R. Co.*, 177 U.S. 51, 61 (1900)).

[19] The Orders Appointing Conservator (October 31, 1985, Pet. App. E and November 26, 1985, Jt. App. p. 8-22), and Liquidator (February 24, 1987, Pet. App. E p. 119a-121a and Jt. App. p. 23-34), the Supplemental Order Appointing Liquidator and Restraining Order (March 5, 1987, Pet. App. E p. 122a-126a), the Final Order of Rehabilitation (April 25, 1990, Jt. App. p. 64-72), the Order Approving Insurance Commissioner's Final Liquidation Dividend Plan, Establishing Final Claims Bar Date for Contingent, Unliquidated and/or Undetermined Claims and Related Orders and Setting Hearing Date (December 28, 1994, Jt. App. p. 135-142), all reiterate the Receivership Court's assumption of sole and exclusive jurisdiction. With the exception of the Order Approving Final Liquidation Dividend Plan, these orders are all final and have not been challenged at any level. Allstate may not now complain about provisions of orders of which it had notice and failed to seek review. *Underwriters Nat'l Assurance Co. v. North Carolina Life & Acc. & Health Ins. Guar. Ass'n*, 455 U.S. 691, 703-10 (1982) [hereinafter *UNAC*].

injunctions also prohibit the obtaining of preferences, judgments, attachments or liens against the assets.[20]

8. Reinsurance Recoverables occupy a special place under the California Insurance Code and that of all other states. Efficacious reinsurance is of special importance in the property and casualty insurance business because of the solvency requirements and financial accounting provisions of California insurance law and that of other states. Under the statutes, insurers must meet certain financial standards and maintain certain capital and surplus in order to issue policies to the public.[21] Each policy issued assumes liabilities against which the insurer must reserve. This increase in reserves creates a resulting decrease in capital and surplus. Thus, in the normal course of business, the more risk an insurer places on the books, the more strain there is upon its surplus. Because of this, insurers, particularly those who underwrite "long tail" liabilities,[22] would eventually be unable to issue new policies unless they acquired further capital and surplus. Reinsurance, however, permits them to do so. *See* Cal. Ins. Code §§ 922.1-922.8.

9. Reinsurance is the insurance of insurance companies. A typical property and casualty insurer, such as one

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[20] These injunctions are contained in the conservation and liquidation orders and are expressly authorized by Cal. Ins. Code § 1020 (Pet. App. D). Cal. Ins. Code § 1058 gives the Receivership Court the jurisdiction to "hear and determine in such proceeding, all actions or proceedings then pending or thereafter instituted by or against" the insolvent. Under *UNAC*, these valid, subsisting and binding orders of the Receivership Court are entitled to full faith and credit and comity.

[21] *See, e.g.*, Cal. Ins. Code §§ 900, 923 and 923.5. Pet. App. D.

[22] For example, liability for long term risks and harm resulting from asbestosis, hazardous waste, construction defects, bodily injury, breast implants, toxic shock syndrome, agent orange, environmental pollution, DES, heart valve, PVC pipe, Dalcon Shield, repetitive task syndrome and other kinds of risks were assumed by the Mission Companies. In fact, the recent California Supreme Court decision in *Montrose Chemical Corp. v. Admiral Ins. Co.*, 10 Cal. 4th 645, 897 P.2d 1, 42 Cal. Rptr. 2d 324 (1995) recognized a "continuous trigger" for such exposures which will impact the Mission Companies' liabilities and that of Allstate.

of the Mission Companies, might have general commercial liability policies with exposure to liabilities running in the hundreds of millions of dollars. Rather than retaining this entire risk, the company reinsures or "lays off" a portion of this liability to other companies. In this manner an insurer might, for example, issue a $20 Million umbrella liability policy, but retain only the first $200,000 of exposure and reinsure the remaining liabilities through various reinsurance agreements.[23] If the original insured paid, for example, a $500,000 premium to MIC for a policy, that premium would be allocated among MIC and its reinsurers in accordance with the reinsurance agreements. In an example such as the one outlined, the reinsurers themselves frequently involve other reinsurers either through "retrocessions"[24] or through various other kinds of arrangements such as stop loss or catastrophe covers. The reinsurance market is international, as can be seen from the various countries in which the Mission Companies' insurers reside,[25] and the original premium is quickly spread over many companies in many states and foreign countries.

10. In normal practice, when a policyholder suffers a covered loss, the original insurer pays the full claim and recovers from the reinsurers their share of the liability.

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[23] If, for example, MIC issued a $20 Million umbrella liability policy, a structure such as the following might result from reinsurance arrangements:

Level of exposure	*Company*
1st layer of $200,000	MIC
2nd layer from $201,000 to $500,000	Reinsurer A
3rd layer from $500,001 to $1 Million	Reinsurer B
4th layer from $1 Million and $1 to $5 Million	Reinsurer C
5th layer from $5 Million and $1 to $20 Million	Reinsurer D

[24] "Retrocession" may be defined as reinsurance of a reinsurer's obligations. Barrons, Dictionary of Insurance Terms 281 (1987).

[25] Argentina, Belgium, Bermuda, Brazil, China, Denmark, Egypt, England, Finland, France, Germany, India, Ireland, Israel, Italy, Japan, Korea, Kuwait, Monte Carlo, the Netherlands, New Zealand, Norway, Singapore, Spain, Sweden, Switzerland, United States, and Venezuela, among others.

The original insurer remains fully liable to the insured for the *entire* loss unless there is some contract provision to the contrary. Such "cut through" provisions are very rare and, normally, the original carrier remains 100% liable to the insured even if it lays off 90% of the risk and pays out 90% of the premium to reinsurers. Significantly, the original insured has no say in, nor necessarily even any notice of, these reinsurance arrangements. Since a policyholder has no cause of action directly against a reinsurer, upon insolvency of the original insurer, *only* the Commissioner, as receiver, can sue the reinsurer to obtain the Reinsurance Recoverables. *Prudential*, 3 Cal. 4th at 1126, 842 P.2d at 52, 14 Cal. Rptr. 2d at 753; *Colonial Am. Life Ins. Co. v. Commissioner*, 491 U.S. 244, 246 (1989); *See also*, Cal. Ins. Code § 922.2.

11. In addition to spreading the risk under the original policy, reinsurance has a salutary and momentous effect upon the insurers' financial statements because the Reinsurance Recoverables may be used, depending on the applicable statute, either as credits or as deductions from liabilities on the insurers' financial statements.[26] In either event, the result is effectively a dollar for dollar increase in the insurers' capital and surplus.[27] This increase in capital and surplus permits the insurer to issue additional policies to the public. More reinsurance permits still further surplus relief and the issuance of more policies to the public. All the while, more and more premium money is spread among more and more reinsurers in dozens or even hundreds of jurisdictions. The insurance-buying public is dependent upon a far-flung reinsurance web which is, in most cases, completely unknown to the general public.[28]

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[26] Accounts receivable, including reinsurance recoverables, are assets of the insurer. *See* Cal. Ins. Code §§ 907, 922.8, 1010-1062, 1064.1-1064.12, Pet. App. D.

[27] Cal. Ins. Code §§ 922.1, 922.15, 922.2, 922.4, 922.5. Pet. App. D.

[28] The entire structure is a house of cards if the original insurer becomes insolvent and the reinsurers cannot be required to pay.

12. Other than actual paid in capital, the primary source for the surplus required to engage in the business of property and casualty insurance is the financial credit booked *because of* the Reinsurance Recoverables. Thus, the nature of, the security for, the accounting for, and the payment of Reinsurance Recoverables are all matters of vital importance to California and the Commissioner in the oversight and regulation of the insurers doing business in California. The Commissioner has broad discretion to adopt rules and regulations to promote the public welfare, and the Commissioner's interpretation of the California insurance statutes is entitled to great deference.[29]

13. The Mission Companies had issued insurance policies to several hundred thousand policyholders in all 50 states and thereby became primarily liable for many billions of dollars in both property and casualty insurance liabilities.[30] Despite this primary liability, the Mission Companies paid many millions of dollars in premium to the reinsurers in consideration of their reinsurance promises and undertakings. But for the financial credits based on the Reinsurance Recoverables permitted by the California statutes referred to above, the Mission Companies could never have issued such a large number of policies to the public. When the Reinsurance Recoverables proved to be unavailable, the Mission Companies became hopelessly insolvent.[31]

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[29] *Ralphs Grocery Co. v. Reimel*, 69 Cal. 2d 172, 177, 444 P.2d 79, 83, 70 Cal. Rptr. 407, 411 (1968).

[30] Certain of the Mission Companies also acted as reinsurers and entered into hundreds of reinsurance transactions ("retrocessions") with reinsurers from all over the world. Under these arrangements, reinsurers ceded business to certain of the Mission Companies.

[31] The fate of the Mission Companies at the hands of their reinsurers is not an isolated situation, but is a matter of general regulatory concern. This can be seen from cases such as *Corcoran v. Ardra Ins. Co., Ltd.*, 842 F.2d 31 (2nd Cir. 1988), and *Doughty v. Underwriters at Lloyd's, London*, 6 F.3d 856 (1st Cir. 1993),

14. When the reinsurers refused to pay, the available cash was soon dissipated and the Mission Companies could neither pay their direct policyholders' claims, nor pay claims from the reinsurance they had assumed. This circumstance created a domino effect and caused severe financial stress upon several other insurance companies. The webs of reinsurance involving the Mission Companies are typical of those involving the rest of the industry. In view of the massive and precarious interdependence among the world's insurers and reinsurers, the underlying issues in the instant litigation far transcend this particular case.

15. The reinsurers' failure to pay was based upon a series of disputes between the Commissioner and the reinsurers regarding the interpretation of California law and its application to these reinsurance arrangements, particularly in the insolvency context. Despite the California Supreme Court decision in *Prudential*, the dispute continues.

16. Over 180,000 claims have been filed in the Receivership Proceedings by policyholders, third party claimants, and state guaranty associations,[32] as well as general

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both of which cases involved an insurance commissioner's attempt to recover reinsurance balances from reinsurers who, having taken their share of the premiums, nevertheless refused to pay their share of the losses. *See also, Grimes v. Crown Life Ins. Co.*, 857 F.2d 699 (10th Cir. 1988), *cert. denied*, 489 U.S. 1096 (1989); *Foster v. Chesapeake Ins. Co., Ltd.*, 933 F.2d 1207 (3rd Cir. 1991); *Corcoran v. Universal Reinsurance Corp.*, 713 F. Supp. 77 (S.D. N.Y. 1989); *Prudential*, 3 Cal. 4th 1118, 842 P.2d 48, 14 Cal. Rptr. 2d 749.

[32] The existence of state insurance guaranty associations ("Guaranty Associations") adds an important dynamic to this analysis. Guaranty Associations for property and casualty companies exist in all states. Their function is to pay policyholder claims when an insurer becomes insolvent. There are various provisions as to the kinds of claims that are covered and there are certain caps on the amounts payable. The funds used to make these payments are public funds because, although they come initially from assessments against the member insurers, the insurers later recoup the money

creditors. Allstate and other reinsurers were among these claimants. To date, the Commissioner has recovered approximately $1.2 Billion from reinsurers, most of which came from settlement agreements. However, the vast majority of those settlements were consummated only after complex litigation, all of which occurred under the auspices of the Receivership Court as the court of original jurisdiction. The instant case involves the interpretation of the various interlocking and/or related reinsurance arrangements and the application of California statutory and case law to them.

17. Unless the Commissioner took affirmative steps to force a turnover of the Reinsurance Recoverables, he could take no effective steps to perform his statutory duties. Accordingly, on December 22, 1986, the Commissioner sued approximately 144 reinsurers.[33] That case, "Gillespie I," was consolidated with the liquidation proceedings and has been, for all relevant purposes, continuously presided over by the Honorable Kurt J. Lewin of the Receivership Court. The instant complaint (hereinafter sometimes called "*Quackenbush*") was filed in June 1990, as a related case, and alleges causes of action identical to those in Gillespie I. Jt. App. pp. 35-63. On August 30, 1990, Allstate removed this action to the federal district court based on diversity grounds under 28 U.S.C. § 1441 and filed a motion to compel arbitration. Jt. App. pp. 73-76 and 77-95.

18. After removal, the Commissioner filed a motion to remand challenging jurisdiction and seeking abstention

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either by taking a direct offset against premium taxes due the state (in which case the state treasury bears the financial burden) or by surcharging policyholders (in which case the burden falls upon the insurance-buying public). When the reinsurers refuse to pay, the public pays. This is one more reason the underlying proceedings involve a vital public concern.

[33] The number of defendants later grew to approximately 300.

under the *Younger*,[34] *Colorado River*[35] and *Burford*[36] abstention doctrines. The district court found it had jurisdiction over the action, and, consistent with the numerous cases deferring to state courts in similar situations involving insolvent insurers,[37] then granted the Commissioner's motion to remand. The district court held that, if it were to adjudicate this action, it would be required to determine an important matter of state law and interfere with the California statutory scheme for the regulation of the insolvency of insurance companies. (Pet. App. B., p. 31a). The district court noted, in particular that this case involved the "critical" claims question of whether a reinsurer is entitled to set-off amounts allegedly owed to the Mission Companies under the provisions of the state statutes (Cal. Ins. Code § 1031). (Pet. App. B, p. 34a). After a thorough review and analysis of the abstention doctrines the district court concluded that *Burford* abstention was called for, holding that:

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[34] *Younger v. Harris*, 401 U.S. 37 (1971) [hereinafter *Younger*].

[35] *Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800 (1976) [hereinafter *Colorado River*].

[36] *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943) [hereinafter *Burford*].

[37] *See, e.g., Doughty v. Underwriters at Lloyd's, London*, 6 F.3d 856 (1st Cir. 1993); *Law Enforcement Ins. Co. v. Corcoran*, 807 F.2d 38, 43-44 (2nd Cir. 1986), *cert. denied*, 481 U.S. 1017 (1987); *Corcoran v. Ardra Ins. Co., Ltd.*, 842 F.2d 31 (2nd Cir. 1988); *Lac D'Amiante du Quebec, Ltee v. American Home Assurance Co.*, 864 F.2d 1033 (3rd Cir. 1988); *Grimes v. Crown Life Ins. Co.*, 857 F.2d 699, 707 (10th Cir. 1988), *cert. denied*, 489 U.S. 1096 (1989); *Hartford Cas. Ins. Co. v. Borg-Warner Corp.*, 913 F.2d 419 (7th Cir. 1990); *Martin Ins. Agency, Inc. v. Prudential Reinsurance Co.*, 910 F.2d 249, 254-55 (5th Cir. 1990); *Barnhardt Marine Ins., Inc. v. New England Int'l Sur. Inc.*, 961 F.2d 529, 531-32 (5th Cir. 1992); *Aims Enters. Inc. v. Muir*, 609 F. Supp. 257 (M.D. Pa. 1985); *Capitol Indem. Corp. v. Curiale*, 871 F. Supp. 205 (S.D.N.Y. 1994); *Mathias v. Lennon*, 474 F. Supp. 949 (S.D.N.Y. 1979); *Metropolitan Life Ins. Co. v. Board of Directors of Wisconsin Ins. Sec. Fund*, 572 F. Supp. 460 (W.D. Wis. 1983); *Mondrus v. Mutual Ben. Life Ins. Co.*, 775 F. Supp. 1155 (N.D. Ill. 1991); and *Sabato v. Florida Dept. of Ins.*, 768 F. Supp. 1562 (S.D. Fla. 1991).

> California has an overriding interest in regulating insurance insolvencies and liquidation in a uniform and orderly manner. If the Court were to adjudicate the Commissioner's reinsurance dispute with Allstate, and specifically the hotly contested set-off issue, then this important state interest could be undermined by inconsistent rulings from the federal and state courts.

Pet. App. B., p. 34a. Accordingly, the district court ordered the remand of this case to the Receivership Court.

19. On appeal by Allstate, the Ninth Circuit Court of Appeals, in a narrowly focused opinion, reversed the decision of the district court. The Ninth Circuit held, first, that review of the remand order in this case was not barred by 28 U.S.C. § 1447(d) and that the remand order based on abstention was a final collateral order reviewable on appeal; and, second, that under decisions of this Court, particularly *New Orleans Pub. Serv. Inc. v. Council of New Orleans*, 491 U.S. 350 (1989) [hereinafter *NOPSI*], a district court *never* has the power to exercise any discretion, regardless of the circumstances presented, to abstain under *Burford* if the suit involves a purely "legal action," as opposed to an action "in equity." The Ninth Circuit wrote: "The Supreme Court's recent, restrictive reading of *Burford*, together with its reaffirmation of the doctrine's equitable predicate, leads us to conclude that a district court may not abstain under *Burford* when the plaintiff seeks only legal relief." (Pet. App. A, p. 12a).

20. On May 19, 1995, the Ninth Circuit denied a petition for rehearing and rejected a suggestion for rehearing en banc. (Pet. App. C). On October 16, 1995, this Court granted the Commissioner's Petition for Writ of Certiorari.

SUMMARY OF ARGUMENT

I. THE COURT BELOW ERRED IN PERMITTING ALLSTATE TO APPEAL THE REMAND ORDER.

The important disputes to be determined in the instant case are Allstate's asserted right to arbitrate and the claimed offset rights. But the subject remand order itself made no determination other than the decision to remand. In *Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336, 352-53 (1976), this Court held squarely that a remand order which does not determine even the forum in which the dispute will ultimately be decided is not subject to an appeal and can only be reviewed by mandamus.

The Ninth Circuit decision below nevertheless held that the remand order in this case is a final collateral order within the meaning of *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949), and is, therefore, appealable under *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983). This interpretation of *Moses H. Cone* and *Cohen* places the court below, erroneously, in conflict with this Court's decision in *Thermtron*.

Neither *Moses H. Cone* nor *Cohen* involved a remand order or abstention. Instead, *Moses H. Cone* involved a stay of a federal action solely because there was a pending state court action, and *Cohen* presented a very special situation in which the federal district court refused to apply a New Jersey statute that would have required plaintiff to post pre-trial security. In *Cohen*, the defendant was about to be forever denied a valuable and important right separate from, and collateral to, the merits of the suit. That case therefore fell into a "small class" of decisions which affect collateral rights too important to be denied review and too independent of the cause of action to require deferral of appellate consideration until the whole case is adjudicated. The instant case does not present sufficiently similar facts to justify application of the "final collateral order" rule.

The decision below in *Quackenbush* stands or falls on the legitimacy of the view that the decision to remand, *by itself*, sufficiently affects an important right that is completely separate from the merits and that is too important to be denied review at the conclusion of the case. To accept this as a proper view would permit *all* remand orders to be appealable unless they come within the bar of 28 U.S.C. § 1447(d). *See Thermtron*, 423 U.S. 336. Adoption of this rule would substantially increase the burden on the federal appellate system.

It is significant that the *Quackenbush* remand order did not place any party "out of court" any more than any other remand order based on abstention principles. Moreover, under *Thermtron*, the remand order remains, in proper circumstances, reviewable in the federal system by mandamus (or, if both trial and appellate courts concur, by interlocutory appeal under 28 U.S.C. § 1292(b)).

Because the district court remanded without reaching the issue of either arbitrability or offset, all issues remain open for initial resolution in state court. If arbitration is allowed, the issue will be moot; if it is denied, then Allstate retains such rights as it may now have to obtain a review in federal court of any federal issues raised.

Since *Thermtron*, this Court has decided a number of other cases applying the *Cohen* doctrine. These include *Lauro Lines s.r.l. v. Chasser*, 490 U.S. 495 (1989), and *Digital Equip. Corp. v. Desktop Direct*, 511 U.S. ——, 114 S. Ct. 1992 (1994). As discussed below, the natural consequence of *Thermtron* and these latter cases is to hold that the instant case utterly fails the collateral order test.

It fails for several reasons. First, it does not present a conclusive determination of an important disputed question in that it has not even determined in what forum the case will proceed. Second, it does not determine an important and unsettled question of controlling law completely separate from the merits; it simply involved the exercise of the district court's discretion. Third, it is not

"effectively unreviewable" on appeal in the sense of meeting the *Cohen* requirements because among other things, Allstate cannot show that it will never have recourse again to federal courts. Under these circumstances, the subject order fails at least one essential prong of the test, in which case it fails the test.[38]

II. THE COURT BELOW ERRED IN REVERSING THE REMAND ORDER ON THE GROUNDS THAT THE DISTRICT COURT HAD NO DISCRETION TO ABSTAIN IN A CASE INVOLVING AN ACTION AT LAW.

The decision below attempts to superimpose the ancient dichotomy between "actions at law" and "suits in equity" on the administration of the abstention doctrine. This Court has never held that abstention is automatically precluded where the underlying action is one at law, and should not do so now.

The imposition of the law/equity distinction upon abstention doctrines would be inconsistent with modern procedure embodied in the provision of Rule 2 of the Federal Rules of Civil Procedure, which merges law and equity into one form of action known as a "civil action." District courts are not required to grant or withhold rights or remedies based upon the form of the action pleaded. *Ross v. Bernhard*, 396 U.S. 531 (1970).[39] Thus, the rule below would improperly restrict the powers and prerogatives of the district courts and undermine the effect of the Federal Rules of Civil Procedure.

This Court has permitted abstention in cases of law. *See, e.g., Louisiana Power & Light Co. v. Thibodaux*,

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[38] *See Coopers & Lybrand v. Livesay*, 437 U.S. 463 (1978); *Lauro Lines*, 490 U.S. 495; *Digital Equip.*, 114 S. Ct. 1992, all discussed below.

[39] *See also*, Dan Dobbs, *Dobbs Law Of Remedies* (2d ed. 1993) Vol. 1 Section 2.6, p. 148: "So today the judge deciding . . . [a] case may apply rules that originated in equity because those are the rules that govern the facts; it will not be necessary to ask whether the court sits as an equity court or a law court because it *always sits as both* (emphasis added)." *Id.* at 150 (citing *Ross*, 396 U.S. 531).

360 U.S. 25, 28 (1959); *Fornaris v. Ridge Tool Co.*, 400 U.S. 41 (1970); *United Gas Pipe Line Co. v. Ideal Cement Co.*, 369 U.S. 134 (1962); *Clay v. Sun Ins. Office, Ltd.*, 363 U.S. 207 (1960); *Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100, 102 (1981); *Langnes v. Green*, 282 U.S. 531 (1931). Thus, it has recognized that abstention doctrines should be rooted, not in an obsolete distinction, but in the deeper policy considerations derived from principles of federalism.

Once a district court's jurisdiction is invoked in a "civil action," the court should be permitted to exercise its discretion to grant any relief legitimately requested by a party. Abstention is the exercise of the court's "equitable discretion," *Burford*, 319 U.S. 315 at 317-18, or its "equitable restraint." *See Fair Assessment*, 454 U.S. at 108; *Baggett v. Bullitt*, 377 U.S. 360 (1964). Thus, a motion to remand on abstention grounds should be viewed as invoking the equitable powers of the district court to order abstention, thereby permitting an order of remand regardless of the formal character of the underlying dispute.

This Court has previously recognized an abstention-like doctrine for insurance insolvency proceedings and for those relating to building and loan companies. *Penn Gen. Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935); *Pennsylvania v. Williams*, 294 U.S. 176 (1935). These cases recognize the special status of state court insolvency proceedings and the propriety of federal court deference to those proceedings. The Court reasoned that even though the district court had subject-matter jurisdiction, the discretion of the court was properly invoked by a motion to relinquish that jurisdiction in favor of the statutory administration of the insolvency in state court.

The Ninth Circuit rule would disregard principles of federalism and interfere with the police power of the states as exercised in the regulation of the business of insurance. The rule would subordinate the Congressional intent, as expressed in the McCarran-Ferguson Act and in exemption of insurance companies from treatment as

debtors under federal bankruptcy laws, to the equity/law dichotomy of a prior era. To hold that principles of judicial federalism may *never* be advanced in a case where the underlying cause of action is one "at law" would needlessly and improperly hinder the administration of justice.

The rule below would also disrupt California's interest in an integrated system of insurance regulation and its ability to further its public interest and protect policyholders in the case of insurer insolvency or delinquency. The Mission Companies have been subject to state court proceedings for approximately 10 years. The Receivership Court has issued a number of orders assuming sole and exclusive jurisdiction. The California statutes mandate that claims against the insolvents' estates will be filed in the Receivership Proceedings and adjudicated by the Commissioner, subject to review of the Receivership Court. The marshaling of assets, particularly sums due from reinsurers, and the adjudication of claims are core functions of the state proceedings which would be disrupted if the Commissioner is subjected to litigation in multiple courts or if Allstate and other claimants are permitted to file claims under the state statutes and then remove them to federal courts for adjudication.

ARGUMENT

I. THE COURT BELOW ERRED IN PERMITTING ALLSTATE TO APPEAL THE REMAND ORDER.

The district court's remand order, based on its determination that abstention was appropriate, was not an appealable order under the precepts of appealability that have been laid down by this Court. The remand order did not terminate the case, and since the question of the arbitrability of the issues presented was not resolved, it did not even determine the forum in which the merits of the case would be adjudicated. The Ninth Circuit's view that the decision to remand is, by itself, a proper subject of appeal was squarely rejected by this Court in *Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336, 352-53 (1976), in which the Court stated that a

remand order is not reviewable on appeal, but only, in appropriate cases, on writ of mandamus.[40]

Despite this controlling authority, the Ninth Circuit held that the remand order was an appealable collateral order under the doctrine of *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949), as interpreted in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983). This reasoning is flawed, and its acceptance would ignore the finality requirement and unduly burden the federal appellate courts.[41]

The *Cohen* case itself is plainly distinguishable from the instant case. In *Cohen*, which did not involve an issue of abstention or remand, a federal district court sitting in diversity held inapplicable a statute of New Jersey, the forum state, requiring certain complainants in a stockholder derivative action to post security for the corporation's reasonable expenses of litigation at the outset of the suit. Since the district court's order meant that the corporation might be forced to endure an entire trial

[40] Both the First and Second Circuits, in well-reasoned opinions, have taken a position directly contrary to that of the court below. *See, e.g., Minot v. Eckardt-Minot*, 13 F.3d 590 (2nd Cir. 1994) (holding, in a case very similar to this one, that a remand order that fails even to determine the forum for adjudication of the dispute is not appealable); *Corcoran v. Ardra Ins. Co., Ltd.*, 842 F.2d 31 (2nd Cir. 1988) (holding, again in a case almost identical to this one, that a district court's remand order was reviewable only on petition for mandamus); *Doughty v. Underwriters at Lloyd's, London*, 6 F.3d 856 (1st Cir. 1993) (same); *see also, Traveler's Ins. Co. v. Keeling*, 996 F.2d 1485 (2nd Cir. 1993) (to the same effect).

[41] In reaching its conclusion, the court below followed its own precedent, *e.g., Pelleport Investors, Inc. v. Budco Quality Theatres*, 741 F.2d 273 (9th Cir. 1984). At the same time, the Ninth Circuit conceded that this precedent was difficult (if not impossible) to reconcile with other precedent in the Ninth Circuit holding unappealable decisions to remand pendent state claims after dismissal of the attached federal claims. *See, e.g., Executive Software N. Am. v. United States Dist. Court*, 24 F.3d 1545, 1562 (9th Cir. 1994). *See* Pet. App. A, p. 7a, n.7.

without the benefit of the security required by state law, the failure to permit an appeal would have left the corporation without any recourse. No post-trial reversal could remedy the fact that the trial would have already occurred without the posting of the security. Thus, the risk of being unable to recover the costs—a risk the state statute was designed to avoid—would irreparably have occurred by the end of the trial. Under these circumstances, the Court concluded that the denial of security "finally determine[d]" a claim of right too important to be denied review. *Cohen*, 337 U.S. at 546.

In the instant case, the circumstances are very different. The relevant state law in *Cohen* would either be applied before trial or not at all. Here, the order of remand resolves neither the issue of arbitrability (which will determine the forum where the merits are to be initially adjudicated) nor the dispute regarding Allstate's claimed offsets.[42] In *Quackenbush*, the district court simply remanded to state court the *same* case that began there. Thus, unless this Court is willing to decide that the solitary action of abstaining and ordering a remand is completely sufficient to meet the *Cohen* test,[43] then the

[42] As the First Circuit stated in *Doughty*: "The remand order at issue here does not pass muster under *Cohen*. The salient legal question that stands separate and apart form the merits in this case—that is, the 'collateral' issue—is whether the parties' overall dispute should be resolved in arbitration. The district court's ruling did not conclusively determine this issue. . . . Instead, the collateral issue remains an open matter—a matter the state court must yet decide. We agree with the Second Circuit that, to come within the collateral order rule, a decree must definitively resolve the merits of the collateral issue, not merely determine which court will resolve it." *Doughty*, 6 F.3d at 863.

[43] "First, the order must 'conclusively determine the disputed question.' Second, it must 'resolve an important issue completely separate from the merits of the action.' Third, it must be 'effectively unreviewable on appeal from a final judgment.' If the order fails any one of these requirements it is not appealable under the collateral order exception." *Gulfstream Aerospace Corp. v. Mayacamas Corp.*, 485 U.S. 271 (1988) (citing *Coopers & Lybrand v. Livesay*, 437 U.S. 463 (1978)). *See also, Lauro Lines s.r.l. v.*

instant case cannot come within the collateral order rule.[44] The only "harm" claimed by Allstate is its claimed interest in avoiding litigation in a state court rather than a federal one. This is not sufficient under either *Cohen* or more recent decisions of this Court.

Cohen presented the quintessential situation where an important issue of controlling law was unjustly relegated to a legal cul de sac from which it could only be rescued by the collateral order doctrine. Thus, this Court was presented with a compelling situation warranting an exceptional remedy. One would not reasonably expect a case presenting such compelling circumstances to occur as an everyday matter. However, remands do routinely occur; and logic alone dictates that remands cannot fall into the "small class" of cases for which the narrow exception permitted by *Cohen* was intended.

This Court has said the collateral order rule is intended to be "narrow" and "exceptional," but the Ninth Circuit's approach would render the rule broad and common. To expand the *Cohen* rule so that the single act of remanding on abstention grounds would meet all three prongs, even though no other determination is made, would permit what is supposed to be a "narrow exception" to "swallow the general rule." [45]

At this stage of this case, Allstate can only claim a *possibility* that it will be required to litigate in state court, because its motion to require the offset dispute to be arbi-

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Chasser, 490 U.S. 495 (1989); *Digital Equip. Corp. v. Desktop Direct*, 114 S. Ct. 1992 (1994).

[44] Furthermore, Allstate has not shown that it will lack recourse to federal court, if appropriate, at a later stage of this litigation.

[45] If the district court had applied the New Jersey statute but set a very low bond, this Court would not have held the order appealable. Similarly, if *Cohen* had been a remand case and proceeded under state law, the narrow circumstance that created the conundrum would not have occurred. Indeed, it was the failure of the district court in *Cohen* to accord appropriate deference to state law which created the problem in the first place.

trated remains pending. If the motion is granted, then Allstate will achieve its preferred forum—arbitration. If the motion is denied, as Allstate may predict it will be, then a new set of complex issues will arise concerning substantial questions of the proper relation of state and federal law to the issue of whether the arbitration clause can overrule the state statutory scheme,[46] but those issues were not adjudicated below and are not presented here. Consequently, Allstate cannot, at this stage, show that it will have no further recourse to federal court.

Under these circumstances, Allstate receives no support from *Moses H. Cone*. In that case, the petitioner had filed a state court action seeking a declaratory judgment that the respondent had no right to arbitrate a dispute and obtained an *ex parte* injunction (later dissolved by the state court) against the taking of any steps toward arbitration.[47] Thereafter, the respondent filed a *separate* federal court diversity action to compel arbitration, and this Court held that the federal court's order staying its own proceedings pending the outcome of the state proceedings was appealable because (given the inevitable res judicata effect of the *separate* state court action) the federal stay order amounted to a dismissal of the suit "when the *sole* purpose and effect of the stay are precisely to surrender jurisdiction of a *federal* suit to a state court." *Moses H. Cone*, 460 U.S. at 11 n.10. In contrast, *Quackenbush* involves a remand of a state court suit back to state court based upon abstention doctrines.

There are at least two critical differences between *Moses H. Cone* and the present case. First, the federal court proceeding here is not a separate proceeding from that commenced in the state court; it is the *same* proceeding. Second, and closely related, in *Moses H. Cone*, the district court's order staying its hand effectively ter-

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[46] *See e.g., Doughty*, 6 F.3d 856, where this same issue was decided against the reinsurer.

[47] In the instant case, the continuing state court injunctions against litigation in other forms remain in place.

minated the *separate* federal proceeding because the district court had already ruled on the matter, and the state court's decision on the issue of arbitrability would have final and preclusive effect on the separate federal litigation. Allstate cannot show that the instant case is in the same posture because it is not. It remains to be seen how the California courts will rule on the propriety of arbitration given the interplay among the statutory insolvency scheme, the McCarran-Ferguson Act, the Federal Arbitration Act, and the other comity, federalism and public policy issues discussed later in this brief. But these are issues of vital state concern. It would, in any event, be fitting in a removal case that a federal court abstain by remanding in such a circumstance, because potential federal law issues may be mooted. If such issues remain, then Allstate may well have recourse to the federal courts again.

The true posture of this case is that Allstate is not necessarily out of any court; it was simply not granted its desire to litigate in federal court in the first instance [48] and it will, instead, be required to go to its less preferred forum.

The Ninth Circuit decision below relies very heavily on the statements in *Moses H. Cone* that the stay placed that plaintiff out of federal court, but as is pointed out, that is not necessarily so in this case. However, the Commissioner also asserts that the collateral order doctrine should not apply to this case unless Allstate can show more than the bare circumstance that it has been sent back to state court. For example, in *Coopers & Lybrand v. Livesay*, 437 U.S. 463 (1978), the district court refused to certify a class action and the putative representative plaintiff attempted to appeal on the grounds that refusal to cetrify the class action effectively ended the entire case. This Court accepted the argument that this might end the suit, but held that fact insufficient to war-

[48] Of course, Allstate does not want ultimately to litigate in any court, it wants to arbitrate, but this does not change this analysis.

rant an immediate appeal. Accordingly, while the court below has relied on the notion that being "put out of federal court" is *all* that is required to invoke the collateral order doctrine, that cannot have been the Court's intent or else it would have decided *Coopers & Lybrand* to permit an immediate appeal.

Here, the decision to remand was a proper exercise of the trial court's discretion, as is argued in detail below, as to the abstention issues.[49] The dispute on appeal to the Ninth Circuit was only over whether that discretion was properly exercised and was not over a *collateral* issue of *controlling law* in the sense of the *Cohen* doctrine.

This was not a proper basis upon which to invoke the collateral order doctrine in *Cohen*. Indeed, to satisfy the *Cohen* test, the "issue on appeal must involve 'an important and unsettled question of controlling law, not merely a question of the proper exercise of the trial court's discretion.' " [50] The Commissioner asserts that this circumstance is a further ground to deny the applicability of the *Cohen* exception in this case.

In *Lauro Lines s.r.l. v. Chasser*, 490 U.S. 495 (1989), the Court held unappealable the denial of the defendant's motion to dismiss, based on a contractual clause requiring suit to be brought in Italy. The Court held that the third prong of the *Cohen* test, that the dispute as to an important matter be effectively unreviewable on appeal from a final judgment, was not satisfied because the asserted right to have the litigation occur in a particular forum as

[49] Indeed, the issues relating to the remand are sufficiently entangled in the merits that one might question whether they are completely separate from the merits for purposes of the collateral order doctrine. *C.f. Coopers & Lybrand*, 437 U.S. at 469 n.12, regarding the "entanglement" with merits of a class certification decision.

[50] *See, Gulfstream Aerospace Corp. v. Mayacamas Corp.*, 485 U.S. 271, 292; (Scalia, J. concurring and emphasizing this point and also noting that the Court should provide further limiting principles so that the *Cohen* appeals will be "as we originally announced they would be, a small class [of decisions] . . . too important to be denied review.")

opposed to another was not effectively unreviewable. The fact that the appellant would be required to endure a full trial in the disfavored forum was not enough because that right, while not perfectly secured by appeal after final judgment, was adequately capable of vindication at that stage. Referring to the Court's opinions in *Richardson-Merrell Inc. v. Koller*, 472 U.S. 424, 431 (1985) and *Coopers & Lybrand*, the Court said: "We have held that to fall within the *Cohen* exception, an order must satisfy *at least* three conditions: It must 'conclusively determine the disputed question,' 'resolve an important issue completely separate from the merits of the action,' and 'be effectively unreviewable on appeal from a final judgment.'" *Lauro Lines*, 490 U.S. at 498 (emphasis added).

The Court did not expand on its reference to the existence of "at least" three conditions, but perhaps this was intended to emphasize that the test is not intended to be a mere "fill-in-the-blanks" test with only three blanks that can be satisfied with the same entry in each blank. This highlights the question of whether the Court ever intended that a single remand order such as the one in this case could satisfy all possible requirements. The Ninth Circuit rule would permit the *Cohen* test to be satisfied with the three "blanks" filled with the *same* condition: "the district court remanded the case." But the real issues involved in the instant remand were the exercise of the court's discretion and Allstate's preferred choice of forum. If the right to be sued in a favored forum was insufficient in *Lauro Lines*, there is no good reason to find it sufficient in this case even if the district court's determination otherwise met the first and second prongs, which it does not.

These observations aside, the concurring opinion in *Lauro Lines* emphasizes that in *Cohen* the Court required that the rights in question be "*too important* to be denied review." *Lauro Lines*, 490 U.S. at 498. This concept of importance was not illuminated in *Moses H. Cone*, but it was discussed further by the Court in *Digital Equipment*, 114 S. Ct. 1992.

In *Digital Equipment*, this Court reaffirmed that choice of forum issues are insufficient to satisfy *Cohen*, and held that "the collateral order doctrine is best understood not as an exception to the "final decision" rule laid down by Congress in Section 1291, but as a "practical construction of it," and that the doctrine applies to "only those district court decisions that are conclusive, that resolve important questions completely separate from the merits, and that would render such important questions effectively unreviewable on appeal from final judgment in the underlying action." *Id.* at 1995. This language, and the discussion at page 2001, appear to incorporate the element of "importance" into both the second and third prongs of the *Cohen* test. Whether the element of importance is a key to satisfying both the second and third prongs or only the third is somewhat academic, since to fail one prong is to fail the test. In either case, the Ninth Circuit view is inconsistent with this Court's decisions. It therefore follows that the Ninth Circuit has erred and that a remand order would not meet the *Cohen* test even if it did select the ultimate forum because forum preference is of insufficient "importance" to satisfy the *Cohen* test.

In *Digital Equipment*, this Court also said that "we have also repeatedly stressed that the 'narrow' exception should stay that way and never be allowed to swallow the general rule."[51] Further, under *Thermtron*, Allstate fails the first prong because the remand order does not present a conclusive determination of the disputed question. To begin with, neither arbitrability nor the offset issues were decided. These were the "important" disputes before the court in the *Cohen* sense. This remand order involves solely a question of the proper exercise of the trial court's discretion.

In *Thermtron*, this Court carved out a narrow exception to the express statutory prohibition (in 28 U.S.C.

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[51] *Digital Equip., id.* at 1996 (citing *Richardson-Merrell, Inc. v. Koller*, 472 U.S. 424 (1985)). *See also, Garcia v. Island Program Designer*, 4 F.3d 57, 60 (1st Cir. 1993).

§ 1447(d)) of *any* review of remand orders—an exception that was not only vigorously criticized in the dissenting opinion in that case but that has also met with significant academic criticism.[52] If that narrow exception is not to swallow up the rule, and threaten the integrity of the finality requirement as well, it is essential that appellate review be limited, as the Court stated in *Thermtron* to the extraordinary writ of mandamus; otherwise every remand order not explicitly based on "jurisdictional" grounds will be automatically appealable.

As the court below explicitly recognized, the difference between allowing a district court order to be appealed and permitting review only on mandamus is not simply a matter of semantics. Mandamus is an extraordinary writ that, as this Court has made clear, is not routinely available. At the same time, the availability of mandamus serves to safeguard against manifest abuse of the discretion to order remand on abstention grounds.[53] Thus, the party seeking to litigate in federal court has access to a method of review that protects against egregious error, but does not disrupt the proper relationship between federal trial and appellate courts.

In summary, the opinion below rests on the presumption that the decision to abstain was itself either a final order or is a proper collateral order under *Cohen* to permit filing an appeal as opposed to seeking mandamus. To accept this view would be to consume the rule with the exception. The resulting delay in the process of litigation would have a negative impact upon the administra-

[52] *See, e.g.*, Michael Solimine, *Removal, Remands, and Reforming Federal Appellate Review*, 58 Mo. L. Rev. 287 (1993). Professor Solimine is also critical of a number of lower court decisions, including the Ninth Circuit's decision in *Pelleport Investors, Inc. v. Budco Quality Theatres, Inc.*, 741 F.2d 273 (9th Cir. 1984), that appear to have extended the scope of *Thermtron*. *See*, 58 Mo. L. Rev. 312-15.

[53] The Commissioner maintains that the district court's order in this case was, not only well within its discretionary authority, but was manifestly correct.

tion of justice and place a substantial burden on federal appellate resources.

II. THE COURT BELOW ERRED IN REVERSING THE REMAND ORDER ON THE GROUNDS THAT THE DISTRICT COURT HAD NO DISCRETION TO ABSTAIN IN A CASE INVOLVING AN ACTION AT LAW.

A. The Court Should Not Restrict Abstention Doctrines On The Basis Of The Equity/Law Distinction.

The Ninth Circuit held that a federal district judge has no power under *Burford* to abstain in a case where the underlying action is at law, as opposed to an action in equity.[54] The Ninth Circuit's opinion is clear and crisp. It draws a hard line between areas where judicial discretion exists and areas where there is no discretion. The effect of the opinion below is to preclude abstention entirely with respect to insurance insolvency proceedings where the underlying action is not an action "in equity." If this Court approves such a rule with respect to insurance insolvency proceedings, it will seriously impinge upon the ability of the states adequately to rehabilitate or liquidate insurers.

California's statutory scheme clearly contemplates that there will be a single, integrated proceeding to devise and implement rehabilitation plans, to marshal assets, accept and adjudicate claims, and otherwise to protect policyholders. These functions cannot be meaningfully carried out if the various elements necessary to the process can be spread out over multiple jurisdictions.[55] The decision below will, among other detriments, permit a reinsurer

[54] In this view, the Ninth Circuit is at odds with other circuits. *See, e.g., Wolfson v. Mutual Benefit Life Ins. Co.*, 51 F.3d 141 (8th Cir. 1995); *General Glass Indus. Corp. v. Monsour Medical Found.*, 973 F.2d 197 (3rd Cir. 1992).

[55] *See supra* note 25.

to file claims [56] in the state court proceedings, as mandated by state law, yet effectively remove them for trial to federal court. This result is directly in contravention of the provisions of the California Insurance Code for handling claims.[57]

Indeed, as in *Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100 (1981), Allstate might have filed a damage suit directly in federal court against the Commissioner, as might have several dozen or a hundred reinsurers in multiple district courts. If, in such an event, the district courts were powerless to apply an abstention doctrine, then the entire statutory scheme of California and other states would be rendered ineffective. Whether such suits were cleverly couched in terms of 42 U.S.C. § 1983, as in *Fair Assessment*, or were filed simply on diversity grounds, they would be suits "at law," and the Ninth Circuit decision would absolutely prevent abstention. A receivership court that cannot control the multiple elements of an insolvency case cannot effectively function.

Since this Court has never taken the position that abstention doctrines are to be separated into watertight compartments, it should not now endorse a rule that handcuffs abstention precepts and the important principles of judicial federalism to equity/law distinctions from a prior era.[58] There have been and will continue to be situations in which abstention is justified where the underlying cause of action sounds in law.[59] To forbid even the possibility

[56] Allstate's offset defenses in this litigation are precisely the same claims contained in the proofs of claim filed by Allstate in the Receivership Proceedings.

[57] *See supra* Statement of the Case, ¶ 6, p. 6-8.

[58] Substantially every point this Court made in *Gulfstream*, 455 U.S. 271, 283-87, about why the perpetuation of the *Enelow-Ettleson* rule was insupportable after the merger of law and equity in the federal courts is applicable to the instant case.

[59] Assuming, *arguendo*, that the underlying suit here is one "at law," then this case is a classic example of why abstention should not be completely precluded in such cases.

of abstention in a case "at law" would unreasonably curtail the ability of the judiciary to perform one of its important functions: the striking of a reasoned balance between state and federal courts.[60]

1. *Such A Rule Would Be Inconsistent With Modern Procedure.*

Superimposing the ancient dichotomy between law and equity upon abstention doctrines would be out-of-step with our modern system. Rule 2 of the Federal Rules of Civil Procedure highlights this point. That Rule, by creating "one form of action known as a 'civil action' " in federal courts, resulted in a merger of law and equity and in the abolition of the forms of action. A court's *complete* jurisdiction is invoked by bringing a "civil action" and the court may thereafter grant all appropriate relief. The result of Rule 2 is that law and equity were combined and "nothing turns now upon the form of the action or the procedural devices by which the parties happen to come before the court." *Ross v. Bernhard*, 396 U.S. 531, 540 (1970).[61]

The artificiality of imposing the equity/law distinction upon current procedures, is further demonstrated, for example by: i) Rule 8(e)(2), which permits a party to combine in one civil action as many separate claims or

[60] Concepts such as those discussed in *Younger* concerning the "ideals and dreams of 'Our Federalism' " and the need to respect and preserve concepts which mandate "sensitivity to the legitimate interests of both State and National Government" should not be disassociated by a hard and fast rule that would forbid abstention based on essentially irrelevant notions of the difference between law and equity.

[61] This Court stated: "Under the Rules there is only one action—a 'civil action'—in which all claims may be joined and all remedies are available. Purely procedural impediments to the presentation of any issue by any party, based on the difference between law and equity, was destroyed. . . . under the rules, law and equity are procedurally combined; nothing turns now upon the form of the action or the procedural devices by which the parties happen to come before the court." *Ross*, 396 U.S. at 539-40.

defenses as the party has regardless of consistency and whether based on legal, equitable or maritime grounds; ii) Rule 18, which permits the joinder of all claims without regard to whether they are legal, equitable or maritime, and which also permits the joinder of remedies, with the court authorized to grant relief in accordance with the relative substantive rights of the parties; and iii) Rule 54(c), which provides that the court will give all relief to which a party is entitled, even if the relief was not demanded in the party's pleadings.[62]

Under these circumstances, there is generally no place in federal civil practice for the granting or withholding of rights or remedies based upon the form of the action pleaded.[63] As this Court noted in *Gulfstream*, 485 U.S. at 271, "Suits that involve diverse claims and request diverse forms of relief often are not easily categorized as equitable or legal . . . [and . . . the *Enelow-Ettelson* rule has placed courts] 'in the unenviable position of . . . solving modern procedural problems by the application of labels which have no currency . . . .'" *Id.* at 284. This Court said the *Enelow-Ettelson* doctrine was, among other things, "divorced from any rational or coherent appeals policy." *Id.* at 285. The same would be true of perpetuating the law/equity dichotomy in the abstention doctrines.

2. *Such A Rule Denies The District Court Its Proper Authority.*

Once a "civil action" is properly removed to a district court, that court has those powers and prerogatives given it by the Rules of Civil Procedure.[64] The relief the district

[62] Also, a court may abstain *sua sponte*. *Bellotti v. Baird*, 428 U.S. 132, 143 (1976).

[63] There are still some applications, not relevant to the issues in this case, such as the right to a jury trial. The Seventh Amendment, however, is controlling in this regard. U.S. Const. amend. VII.

[64] In *Atlas Life Ins. Co. v. W.I. Southern, Inc.*, 306 U.S. 563 (1939), even under prior practice, this Court held that the power of the courts to have "cognizance . . . of all suits of a civil nature at common law or in equity" does "*not* define the jurisdiction of the

court may grant is not limited under the Rules by forms or consistency of pleading, by the equity/law distinction, or even by the relief requested. The court may grant complete relief without regard to the form of the pleading and without regard to whether the relief would have been considered equitable or legal under prior law.[65]

It is inconsistent with our current federal procedural system to rule that the district court is barred from exercising its principled discretion in applying abstention doctrines unless the underlying pleadings sound in equity.

3. *This Court Has Not Limited Abstention Doctrines To Equity Suits, Nor Should It.*

Many square-peg/round-hole difficulties would arise by an attempt to force ancient distinctions into a modern system where the underlying proceedings are often combinations of actions at law, actions in equity, and actions pursuant to statutes. Indeed, in the instant case the underlying action is intimately connected with a state statutory scheme and the operation of a highly regulated industry where the Commissioner embodies the police power of the state and acts in an industry long recognized as involving vital public concerns.[66]

district courts as federal courts, in the sense of their power or authority to hear and decide, but prescribes the body of doctrine which is to guide their decisions and enable them to determine whether in any given instance a suit . . . is an appropriate one for the exercise of the extraordinary powers of a court of equity." *Id.* at 568 (citing *Pennsylvania v. Williams*, 294 U.S. 176 (1935) (emphasis added).

[65] Prior to the adoption of the Constitution, the states were far from uniform with respect to the maintenance of the equity/law dichotomy in their courts. This can be seen in Alexander Hamilton's discussion of the right to a jury in civil cases and the nature of the judiciary. The Federalist Nos. 80, 83 (Alexander Hamilton).

[66] The Ninth Circuit itself is fully aware of the need to grant deference to state insurance insolvency proceedings, and it did so in *Morgan Stanley Mortgage Capital v. Insurance Comm'r*, 18 F.3d 790 (1994), in which it approved a district court's dismissal of a diversity action in deference to a pending state court insurance

To be sure there are important factors supporting the exercise of federal jurisdiction, but this Court has also decided that there can be compelling reasons for federal courts to abstain from exercising their jurisdiction in particular circumstances.[67] This Court's decisions regarding abstention have rested upon a full analysis of the case at hand; not upon the mere form of the pleadings.

Although many of the cases in which this Court has ordered or upheld abstention have involved actions in equity, that has not been uniformly the case.[68] Thus, the

insolvency. Circumstantially, *Morgan Stanley* involved a proceeding in the same receivership court as the Receivership Court in *Quackenbush*. The state court had issued very similar injunctions pursuant to the same statutes in order to assume jurisdiction over the assets of Executive Life Insurance Company. The motion filed with the district court in *Morgan Stanley* was virtually the same as that filed in the district court in *Quackenbush*. In *Morgan Stanley*, the particular district court dismissed; in the instant case the district court abstained and remanded, but the jurisdictional issues were essentially the same. In *Morgan Stanley*, the Ninth Circuit held that the district court properly deferred to the Receivership Court due to the various orders of the Receivership Court which assumed the sole and exclusive jurisdiction over the insolvent's assets. In *Quackenbush*, it reversed the remand order. The only material distinction between the two cases appears to be that the Ninth Circuit felt compelled to apply the equity/law distinction to abstention cases because of *NOPSI* and Ninth Circuit precedent, but had no such compulsion where the district court dismissed instead of abstaining. If the district court in this case had dismissed in favor of the Receivership Court, then under *Morgan Stanley*, the Ninth Circuit would apparently have affirmed the district court. These two very different results hinge completely upon the equity/law distinction as applied to *Burford* abstention by the Ninth Circuit. Such a result is inappropriate.

[67] "No one factor is necessarily determinative; a carefully considered judgment taking into account both the obligation to exercise jurisdiction and the combination of factors counseling against that exercise is required." *Colorado River*, 424 U.S. at 818.

[68] *See, e.g., Fornaris v. Ridge Tool Co.*, 400 U.S. 41 (1970); *United Gas Pipe Line Co. v. Ideal Cement Co.*, 369 U.S. 134 (1962); *Clay v. Sun Ins. Office, Ltd.*, 363 U.S. 207 (1960); *Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100, 102 (1981); *Louisiana Power & Light Co. v. Thibodaux*, 360 U.S. 25, 28 (1959); *Langnes v. Green*, 282 U.S. 531 (1931).

fact that a particular prior case involved an equitable proceeding appears to be a *circumstance*, but not a *prerequisite* to the invocation of abstention doctrines in all cases.

Because federal courts have a continuing duty to examine their own jurisdiction and because many abstention cases involve questions as to the district court's jurisdiction, it is no surprise that most, if not all, abstention cases comment on the basis of the court's jurisdiction.[69] The Ninth Circuit deemed the various references in this Court's opinions to a "court sitting in equity," an "equity court" and a "court of equity" in *NOPSI*, *Burford* and *Alabama Pub. Serv. Comm'n v. Southern R. Co.*, 341 U.S. 341 (1951), as statements of interest to impose an absolute limit on abstention to "equity cases" and to bar abstention in suits "at law." To attribute such a restrictive effect to those statements ignores the context in which they were made; the references are more properly viewed as observations as to the source of authority to abstain—as affirmations that the district court had discretion to abstain in the exercise of its traditional powers. Because of the merger of law and equity in the federal courts, a district court *always* has the capacity to exercise its "equitable" powers.[70] Indeed, under Rule 54(c), a court may award equitable relief in a case where the pleadings allege only causes of action "at law."

In *Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100, 102 (1981), the underlying cause of action was unquestionably one at law. Permitting damage suits

[69] The very idea of "abstaining" assumes that the court has a choice. A court can only abstain if it has jurisdiction. *See, e.g., Miller-Davis Co. v. Illinois State Toll Highway Auth.*, 567 F.2d 323, 325-26 (1977).

[70] *See supra* note 39. *See also*, discussion *infra* part II.A.5 for the argument that even prior to the merger of law and equity in the federal system, the district court could nevertheless exercise its equitable discretion to abstain regardless of the underlying nature of this litigation.

in federal courts against state taxing officials would have had very serious adverse consequences on the administration by the states of their tax laws.[71] *Fair Assessment*, 454 U.S. at 108. The district court granted a motion to dismiss on grounds that it referred to as "comity" under this Court's decision in *Younger*. In this Court's own opinion, it relied on comity and the doctrine of equitable restraint in a case "at law." *Id.* at 116.[72] The vital state interests of insurance regulators are deserving of the same deference and comity as are the concerns of state taxing authorities.[73]

Another relevant decision is *Ankenbrandt v. Richards*, 504 U.S. 689 (1992), an action "at law" in which this Court focused initially upon the question of whether there was federal jurisdiction over domestic relations cases. After affirming the long-standing "domestic relations" ex-

[71] This would be equally true regarding insurance regulation.

[72] Justice Brennan, in his concurring opinion, while suggesting that abstention doctrines had been applied only in equity actions, *id.* at 120 n.4, acknowledged that in *Clay v. Sun Ins. Office, Ltd.*, 363 U.S. 207 (1960), the underlying action was one at law. He also cited this Court's statement explaining its decision in *Louisiana Power & Light Co. v. Thibodaux*, 360 U.S. 25, 29 (1959), without specifically commenting on the fact that the underlying action in *Thibodaux* was also at law. Further, after referring to abstention as an "application of the comity principle," *Fair Assessment*, 450 U.S. at 120 n.4, he later said that "[t]his is not to suggest that there is no occasion to apply principles of comity in actions at law." *Id.* at 121 n.5. Justice Brennan then approved the action of the district court, but on the basis of the failure to exhaust administrative remedies, acknowledging this is an exercise of comity. Given his earlier statement that abstention is similarly an application of the principle of comity, the philosophical basis of *both* the majority and concurring opinions was clearly rooted in principles of federalism, comity, and deference to vital state interests.

[73] "Few public interests have a higher claim on the discretion of a federal chancellor than the avoidance of needless friction with state policies, whether the policy relates to the enforcement of the criminal law (citations omitted) or the administration of a specialized scheme for liquidating embarrassed business enterprises. . . ." *Moore v. Sims*, 442 U.S. 415, 428 (1970) (citing *Pennsylvania v. Williams*, 294 U.S. 176 (1935), discussed below).

ception, which divests federal courts of diversity jurisdiction over suits for divorce and alimony decrees, the Court held that the federal courts did have jurisdiction over the particular dispute, which involved the allegation that the respondents had committed torts against the Ankenbrandt's children. *Id.* at 704.

This Court then addressed the issue of "whether, even though subject-matter jurisdiction might be proper, sufficient grounds exist to warrant abstention from the exercise of that jurisdiction." *Id.* Upon this second-step analysis, the Court determined that on the facts of the case, the necessary factors to warrant abstention under *Younger*, *Burford* or *Colorado River* did not exist and, therefore, declined to sanction abstention. But the Court did not indicate any doubt that abstention would have been warranted if appropriate factors had existed. The circumstance that the underlying suit was an action at law was not even mentioned as a factor militating against abstention. To the contrary, the Court specifically acknowledged that *Burford* abstention might be appropriate in certain domestic relations cases, and, since the Court engaged in an abstention analysis, it seems to follow that the equity/law issue was not deemed material. *Id.* at 705-06.

Similarly in *Thibodaux*, as noted above, the underlying suit was "at law," and the majority, in speaking of prior situations in which the Court *required*, not merely sanctioned, district courts to abstain, said:

> These prior cases have been cases in equity, but they did not apply a technical rule of equity procedure. They reflect a deeper policy derived from our federalism. We have drawn upon the judicial discretion of the chancellor to decline jurisdiction over a part or all of a case brought before him . . . Although an eminent domain proceeding is deemed for certain purposes of legal classification a "suit at common law" . . . it is of a special and peculiar nature . . . it is intimately involved with sovereign prerogative.

Thibodaux, 360 U.S. at 27 (internal citations omitted).[74]

[74] The dissent did not object on the grounds that abstention was barred in an action at law even though it was expressly noted that

In another decision, *Langnes v. Green*, 282 U.S. 531 (1931), an action involving damages for personal injuries, the federal court entered a restraining order preventing a state trial in a parallel proceeding. This Court held unanimously that the district court did have jurisdiction, but should have deferred to the state court. The Court stated, *inter alia*, that "the question which arose was not one of jurisdiction, but, . . . was whether as a matter of discretion that jurisdiction should be exercised to dispose of the cause." *Id.* at 541. The Court observed that the term "discretion" denotes the absence of a hard and fast rule. This observation focuses the issue in the instant case. Here, the court below has attempted to impose a hard and fast rule, but the very principle of abstention requires the exercise of the court's sound discretion. To lay down a flat rule that no court can ever abstain in an action "at law" is not only inconsistent with the concept of discretion, but also ignores a number of cases in which this Court has either sanctioned, or actually required, the exercise of such discretion in such an action.

4. *Abstention Should Be Viewed As An Exercise Of The Equity Aspect Of The Court's Merged Jurisdiction.*

Under the Federal Rules of Civil Procedure, once jurisdiction attaches, the Court may grant any relief legitimately requested by a party. Thus, if a party seeks to transfer venue, to obtain a more definite statement, a delay in the trial, summary judgment, a protective order, or any other relief permissible, then upon proper motion, the district court has the power to grant it without first

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the underlying suit *was* a suit at law. Instead, the dissent was based on arguments that the grounds for abstention were absent. *Id.* at 33. To be sure, there may be fewer circumstances in which abstention grounds will exist in an action for damages than in one in which the *state* is being enjoined. That possibility, however, does not *mandate* a general rule absolutely forbidding abstention in cases "at law" no matter what the impact on "Our Federalism" or other abstention concerns. An insurance insolvency proceeding under the guidance of the Commissioner and a state receivership court involves the state's "sovereign prerogative."

performing an analysis as to whether the underlying remedy sought is legal or equitable. Similarly, there is no reason why the court needs to determine the nature of the underlying pleading prior to granting a motion to remand or to dismiss on abstention principles.[75] If the transcendent factors recognized by this Court as warranting abstention exist in a given case, then abstention should be granted on the basis of those principles without regard to the historical nature of the particular cause of action pleaded.

Even if a district court must be "sitting in equity" in order to abstain, the determination should be made on the basis of the relief sought in the motion, not on the nature of the complaint in the case. Since abstention is the discretionary exercise of the court's "equity powers,"[76] then a court *is* "sitting in equity" when it abstains. If, in an action for damages, a federal court issues an injunction against a state court damage suit, one would not doubt that the court has exercised its equity power despite the fact that *both* the federal and state court suits are actions "at law."

Abstention doctrines are based upon federalism and comity, not the details of pleading.[77] If this Court adopts the rule of the decision below, then, not only will it depart from its prior decisions, but it will thrust the application of abstention doctrine into a morass in which district courts struggle to apply an antiquated equity/law dichot-

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[75] *See generally*, David Shapiro, *Jurisdiction and Discretion*, 60 N.Y.U. L. Rev. 543, 550 (1985).

[76] *Baggett v. Bullitt*, 377 U.S. 360, 375 n.11 (1964); *see also*, *Fair Assessment*, 454 U.S. at 108.

[77] In *NOPSI*, for example, this Court said that it inquires "into the substantiality of the State's interest in its proceedings we do not look narrowly to its interest in the *outcome* of the particular case . . . [r]ather, what we look to is the importance of the generic proceedings to the State. In *Younger*, for example, we did not consult California's interest in prohibiting John Harris from distributing handbills, but rather its interest in 'carrying out the important and necessary task' of enforcing its criminal laws." *NOPSI*, 491 U.S. at 365.

omy to modern problems and modern complex litigation.[78] Eventually, this Court would need to rewrite abstention doctrines to provide standards for determining when the underlying causes of action are in equity or when a sufficient level of equitable causes of action exist in a multiple count lawsuit to warrant a district court's even beginning a reasoned analysis to determine whether it should abstain.

A court should never shirk its duty, but this case presents a powerful question of where that duty lies. The protection of judicial federalism is one of the important duties of all federal courts.[79] The irony of the decision below is that fundamental principles of federalism would take a back seat to the perpetuation of the equity/law dichotomy. As discussed in Section B, below, the instant case serves to highlight this irony and to reveal its basic flaw.

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[78] *See* David Shapiro, *Jurisdiction and Discretion*, 60 N.Y.U. L. Rev. 543, at 570-74.

[79] While the members of the court disagreed as to the application of the Commerce Clause in *United States v. Lopez*, 514 U.S. ——, 115 S. Ct. 1624 (1995), there does not appear to be any division as to the basic importance of the principles of federalism. Quoting from *Gregory v. Ashcroft*, 501 U.S. 452, 458 (1991), the opinion of the Court states: "Just as the separation and independence of the coordinate branches of the Federal Government serves to prevent the accumulation of excessive power in any one branch, a healthy balance of power between the States and the Federal Government will reduce the risk of tyranny and abuse from either front." *Lopez*, 115 S. Ct. at 1626. In the concurring opinion of Justice Kennedy, with whom Justice O'Connor joined, it is said: "Were the Federal Government to take over the regulation of entire areas of traditional state concern . . . the boundaries between the spheres of federal and state authority would blur and political responsibility would become illusory. (citations omitted) . . . In the past this Court has participated in maintaining the federal balance through judicial exposition of doctrines such as abstention. . . ." (citations omitted) *Id.*, 115 S. Ct. at 1638-39. In his concurring opinion, Justice Thomas states: "[O]ur cases are quite clear that there are real limits to federal power (citations omitted) . . . Indeed, on this crucial point, the majority and Justice Breyer agree in principle: the Federal Government has nothing approaching a police power." *Id.* at 1642.

5. *This Court Has Previously Recognized An Abstention-Like Doctrine In Insurance And Thrift Insolvencies, Based Upon An Analysis Consistent With The Commissioner's Contentions.*

This Court has previously recognized an abstention-like doctrine applicable to insurance and thrift insolvency proceedings. In these cases the Court recognized the district court's discretion to relinquish jurisdiction after that jurisdiction had been properly invoked.

In *Penn Gen. Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935), an action to appoint a receiver and liquidate an insurer was filed in federal district court. Thereafter, an essentially identical action was filed in the Pennsylvania state court. This Court confronted two issues: i) whether the district court had jurisdiction at all; and ii) whether, if it had jurisdiction, it should defer to the state court proceedings.

In a first-step analysis, this Court held that the district court did have subject-matter jurisdiction under its equity jurisdiction and that the court first assuming jurisdiction in an *in rem* or *quasi in rem* action may maintain and exercise that jurisdiction to the exclusion of the other court. *Id.* at 195. This Court then held that since the district court suit was filed first, the district court had the power to retain jurisdiction. *Id.* at 197. Notwithstanding this finding, this Court then concluded that since the "end sought by the liquidation in the state court is the liquidation of a domestic insurance company by a state officer" and since there was no showing that the interests of creditors and shareholders would not be protected by the state court, the case was a "proper one for the district court, in the exercise of judicial discretion, to relinquish the jurisdiction in favor of the administration by the state officer." *Id.* Thus, the Court effectively acknowledged an abstention doctrine applicable to state court insurance insolvency proceedings even prior to the *Railroad Comm'n of Texas v. Pullman Co.*, 312 U.S. 496 (1941), *Younger*, *Burford* or *Colorado River* decisions.

In a companion case, *Pennsylvania v. Williams*, 294 U.S. 176 (1935), this Court faced substantially the same issues as in *Penn General*, but with respect to receivers of an insolvent building and loan association.[80] This Court observed that the underlying action to appoint a receiver and liquidate the company was an action in equity and that the district court therefore had the jurisdiction to entertain the suit. *Id.* at 183. The Court also held that, since there were state statutes with elaborate provisions for such a liquidation through the action of a state officer, "the discretion of the district court, *invoked by the petition of the commonwealth*, should have been exercised to relinquish the jurisdiction in favor of the statutory administration of the corporate assets by the state officer." *Id.* at 183 (emphasis added). As shown by the italicized phrase, the trigger to the exercise of the district court's discretion was not the nature of the underlying suit, but the nature of the relief requested by the commonwealth—the motion to relinquish jurisdiction.[81] The jurisdiction of the court was invoked in the first instance by the underlying suit, but the invocation of the court's equity power, jurisdiction having attached, was invoked by the nature of the motion seeking the relinquishment of jurisdiction.

These two cases establish important precedent.[82] First, they recognize an abstention doctrine applicable to insurance companies and building and loan companies on the grounds that there were comprehensive state court statutory schemes to be administered by a state officer in a state court. Second, though the underlying liquidation proceedings were held to be equitable in nature, that fact

[80] Building and loan companies, like insurance companies, cannot be debtors in federal bankruptcy proceedings. *See* 11 U.S.C. § 109(b)(2); *Williams*, 294 U.S. at 179.

[81] The referenced petition of the Commonwealth was a petition for leave to intervene and for an order directing the surrender of the assets of the defendant association to the state secretary of banking.

[82] *See also, Gordon v. Washington*, 295 U.S. 30 (1935), and *United States v. Bank of New York & Trust Co.*, 296 U.S. 463 (1936).

was key to the analysis of whether the federal court had jurisdiction at all, but *not* to the exercise of the discretion to abstain: "[i]n such circumstances the discretion of the district court, invoked by the petition of the commonwealth [essentially, to abstain], should have been exercised to relinquish the jurisdiction . . . ." *Id.* at 183. In other words, jurisdiction having attached, the court may be regarded as *sitting in equity* [83] if its equitable powers are invoked by a proper request. This is exactly consistent with the appropriate application of the Rules of Civil Procedure discussed above.

B. The Ninth Circuit Rule Would Undermine Principles Of Federalism.

1. *The Abstention Doctrine Should Facilitate The Regulation Of Insurance By The States To Which Congress Has Deferred.*

This Court has long acknowledged that the regulation of the business of insurance is within the police power of the states and that government has always had a special relation to insurance.[84] Congress has the authority to regulate the business of insurance under the Commerce Clause. *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944).[85] But, as this Court noted

[83] Though Rule 2 created one form of action and abolished any need for making the law/equity distinction in the pleadings, principles of equity are still used in fashioning appropriate relief.

[84] *United States Dep't of Treasury v. Fabe*, 508 U.S. ——, 113 S. Ct. 2202 (1993); *Osborn v. Ozlin*, 310 U.S. 53, 65 (1940); *California State Auto. Ass'n Inter-Ins. Bureau v. Maloney*, 341 U.S. 105 (1951); *German Alliance Insurance Co. v. Lewis*, 233 U.S. 389, 411 (1914) ("The cases need no explanatory or fortifying comment. They demonstrate that a business, by circumstances and its nature, may rise from private to be of public concern and be subject, in consequence, to governmental regulation.").

[85] In *South-Eastern Underwriters*, this Court emphasized the extreme importance of insurance to the public. In *German Alliance*, 233 U.S. 389, the Court noted: "The contracts of insurance may be said to be interdependent. They cannot be regarded singly, or isolatedly, and the effect of their relation is to create a fund of

in *Fabe*, Congress enacted the McCarran-Ferguson Act, 15 U.S.C. § 1011, in response to *South-Eastern Underwriters*. *Fabe*, 113 S. Ct. 2202. By the McCarran-Ferguson Act, Congress mandated, at Section 1012(b), that:

> No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance . . . .

Thus, Congress has stayed its hand in the regulation of the business of insurance and deferred to the police power of the states.[86] The application of judicial federalism through the abstention doctrine should be consistent with Congressional intent where that intent has been made plain. In the area of insurance regulation, Congressional intent to defer to state interests is plain; accordingly, the abstention doctrine should be responsive to this goal.

2. *The Ninth Circuit Rule Would Create A Rift In The Application Of Federalism Principles.*

In *Fabe*, this Court acknowledged the importance of insurance insolvency proceedings. Unlike *Fabe*, this case involves no Supremacy Clause issue and no issue involving the federal priority statute, 31 U.S.C. § 3713. But, insofar as issues of judicial federalism are concerned, in-

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assurance and credit, the companies becoming the depositories of the money of the insured, possessing great power thereby and charged with great responsibility." *German Alliance*, 233 U.S. at 414.

[86] It is also significant that the Congress has long exempted insurance companies from the Bankruptcy Act and now the Bankruptcy Code. Under Sections 109(b)(2) and (d) of that Code, insurers may not be debtors under federal bankruptcy laws. These cases are to proceed in state courts even where there is a competing bankruptcy matter. *In the matter of Equity Funding Corp.*, 396 F. Supp. 1266 (C.D. Cal. 1975); *Baldwin-United Corp. v. Garner*, 283 Ark. 385, 678 S.W. 2d 754 (1984), *cert. denied*, 471 U.S. 1111 (1985).

surance insolvency proceedings are intimately connected with the regulation of the insurance industry. Such regulation is traditionally a state enclave and Congress has gone to some length to have it remain so even in the wake of this Court's decision in *South-Eastern Underwriters*, 322 U.S. 533.[87]

Under the Ninth Circuit's rule, the equity/law dichotomy would trump principles of federalism, even in insurance insolvency proceedings, and would establish the rule that the federal courts have no power to protect these principles through the application of the abstention doctrine in cases sounding in law.[88]

3. *The Abstention Doctrines Promote Federalism.*

The opinion below would require a district court to turn its face from judicial federalism in *any* action "at law" even where "difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar," where the "exercise of federal review of the question in a case and in similar cases would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern," and where assumption of jurisdiction in the federal court would disrupt ongoing state proceedings.[89] This view ignores the reality—recognized by this Court in other decisions—that a case not sounding purely in equity can be one calling for abstention. This Court should not approve a rule holding that federal district courts can never exercise their sound

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[87] The McCarran Act was one factor in prompting the Court to abstain in *Colorado River*. The principles behind the McCarran-Ferguson Act are very similar to those behind the McCarran Act.

[88] This would be singularly inappropriate where important state interests are concerned. *See e.g.*, Gordon Young, *Federal Court Abstention and State Administrative Laws from Burford to Ankenbrandt: 50 Years of Judicial Federalism Under Burford v. Sun Oil Co., and Kindred Doctrines*, 42 De Paul L. Rev. 859, 945 (1993).

[89] *See NOPSI*, 491 U.S. at 361 (quoting *Colorado River*, 424 U.S. at 814).

discretion to apply principles of federalism through the abstention doctrine unless the underlying case would have sounded in equity under the equity/law dichotomy.

4. *Application Of The Ninth Circuit Rule In The Instant Case Is Disruptive Of Important State Interests and Interferes With California's Statutory Scheme.*

California's Insurance Code establishes an integrated matrix that would be severely disrupted if vital aspects, such as the conduct of liquidation proceedings and claims processes, are undermined by being subjected to multiple litigation in multiple jurisdictions with varying interpretations of California law and policy.[90]

The basic purpose of state regulation of insurers is to see that an efficacious insurance product is delivered to the public. To serve the public interest, "insurance" must truly be "insurance" and state governments must be permitted to regulate insurance and reinsurance contracts so that they will be effective if the risk insured against is realized. Not only is the basic financial health of individuals and businesses at stake, but so is the confidence of the entire public.[91] Common sense, and a significant number of judicial decisions, strongly support the view that special circumstances supporting abstention are very likely to exist in matters affecting insurance insolvency proceedings.[92]

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[90] Permitting the repetition of a suit such as that in *Fair Assessment* against this Country's insurance regulators with no possibility of abstention would have a deep and dangerous chilling effect on insurance regulation.

[91] *In re Integrity*, 573 A.2d 928, 240 N.J. Super. 480 (Super. Ct. 1990); *In re Executive Life Ins. Co.*, 32 Cal. App. 4th, 344, 375-76, 38 Cal. Rptr. 2d 453, 471, *rev. denied* (1995); *South-Eastern Underwriters*, 322 U.S. 533.

[92] *See, e.g., Penn Gen.*, 294 U.S. 189, 196; *United States v. Bank of New York & Trust Co.*, 296 U.S. 463 (1936); *Princess Lida v. Thompson*, 305 U.S. 456 (1939); *Lion Bonding Sur. Co. v. Karatz*, 262 U.S. 77 (1923); *see also* note 37 *supra*.

It should also be noted that one of the effects of California's statutes, and the terms of the reinsurance agreements themselves, is to transform these contracts from commercial agreements between private parties to regulatory agreements with a state official. *Corcoran v. Ardra Ins. Co., Ltd.*, 657 F. Supp. 1223, 1232 n.6 (S.D.N.Y. 1987). These reinsurance agreements are not merely private contracts, but are subject to the control of the state. *See, e.g., Osborn*, 310 U.S. 53; *Maloney*, 341 U.S. 105. Under California law, Allstate and all others contracting with insurers are deemed to have knowledge of the law and the terms of relevant law and regulations are deemed to be a part of their agreements. *Alpha Beta Food Mkts., Inc. v. Retail Clerk's Union*, 45 Cal. 2d 764, 291 P.2d 433 (1955). When Allstate entered into the reinsurance agreements, it knew it acted in a highly regulated industry. It also knew that the very solvency of the Mission Companies depended upon the performance of its reinsurers, that there were statutory provisions governing the Mission Companies' reinsurance agreements and the Reinsurance Recoverables, and that if the Mission Companies became insolvent, they would be placed into state court insolvency proceedings and that Allstate would be subjected to the state statutory insolvency scheme.[93] Allstate contracted with knowledge of all these factors, but now Allstate wishes to have nothing to do with the Commissioner or the Receivership Court.

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[93] Allstate's reinsurance agreements contain what is known as an "insolvency clause." *See, e.g.*, Jt. App. p. 109-110. In pertinent part this clause is mandated by Cal. Ins. Code § 922.2 and provides: "In the event of insolvency and the appointment of a conservator, liquidator or statutory successor of the ceding company, [the Reinsurance Recoverables] shall be payable to such conservator, liquidator or statutory successor immediately upon demand, with reasonable provision for verification . . . without diminution because of such insolvency or because such conservator, liquidator or statutory successor has failed to pay all or a portion of any claims." (Pet. App. D). In the face of these provisions, Allstate cannot in good faith assert that it did not expect at the time of contracting to be brought into any subsequent state court insolvency proceedings involving the Mission Companies.

Whether the district court was right or wrong in abstaining is not *per se* before this Court. However, it is necessary to focus on the many compelling circumstances that *could* motivate a district court to abstain—and certainly did play a role in this very case—if not prevented from even considering the issue by the decision below. If this Court permits the decision below to stand, then it will force federal courts to ignore cases that present compelling circumstances for abstention unless they first find the underlying matter is purely "in equity." There is no good reason to force the district courts into such straitjackets or to subject state regulators to such an arcane process. There is nothing to commend the imposition of such burdens upon the federal and state systems and there are very good reasons to condemn it.

CONCLUSION

For the reasons discussed above, the judgment below should be reversed and the case remanded with appropriate directions.

Respectfully submitted,

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APPENDIX

APPENDIX A

Rule 2. One Form of Action

There shall be one form of action to be known as "civil action".

Rule 8.

* * * *

(e) Pleading to be Concise and Direct; Consistency.

(1) Each averment of a pleading shall be simple, concise, and direct. No technical forms of pleading or motions are required.

(2) A party may set forth two or more statements of a claim or defense alternately or hypothetically, either in one count or defense or in separate counts or defenses. When two or more statements are made in the alternative and one of them if made independently would be sufficient, the pleading is not made insufficient by the insufficency of one or more of the alternative statements.

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Rule 18. Joinder of Claims and Remedies

(a) Joinder of Claims. A party asserting a claim to relief as an original claim, counterclaim, cross-claim, or third-party claim, may join, either as independent or as alternate claims, as many claims, legal, equitable, or maritime, as the party has against an opposing party.

(b) Joinder of Remedies; Fraudulent Conveyances. Whenever a claim is one heretofore cognizable only after another claim has been prosecuted to a conclusion, the two claims may be joined in a single action; but the court shall grant relief in that action only in accordance with the relative substantive rights of the parties. In particular, a plaintiff may state a claim for money and a claim to have set aside a conveyance fraudulent as to that plaintiff, without first having obtained a judgment establishing the claim for money.

* * * *

Rule 54.

(c) Demand for Judgment. A judgment by default shall not be different in kind from or exceed in amount that prayed for in the demand for judgment. Except as to a party against whom a judgment is entered by default, every final judgment shall grant the relief to which the party in whose favor it is rendered is entitled, even if the party has not demanded such relief in the party's pleadings.